STATEMENT OF
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BEFORE THE
BANKING AND FINANCIAL SERVICES COMMITTEE
U.S. HOUSE OF REPRESENTATIVES
WASHINGTON, D.C.
April 23, 1998
ON
H.R. 219
THE HOMEOWNERS' INSURANCE AVAILABILITY ACT

My name is Rade Musulin. I am Vice President and Actuary of the Florida Farm Bureau Insurance Companies and a member of the Casualty Actuarial Society and the American Academy of Actuaries. My company is part of the Southern Farm Bureau Group, which insures property risks in six southeastern states for members of the Farm Bureau Federation. Our group is exposed to both hurricanes in the Gulf and Atlantic coasts as well as earthquakes in the New Madrid and Savannah River areas.

I serve on the Advisory Council of the Florida Hurricane Catastrophe Fund and participated as a member of an ad-hoc working group directed by Senator Ted Stevens' staff in 1996 on disaster insurance.

I appear before you today on behalf of the Florida Farm Bureau Casualty and the Southern Farm Bureau Casualty Insurance Companies. We are members of the National Association of Independent Insurers, a non-profit property/casualty trade association representing more than 560 insurance companies on whose behalf I also am testifying.

Throughout the country, Farm Bureau Insurance Companies provide many Americans with property insurance coverage through single state or regional companies. Companies like ours are critical parts of the insurance marketplace. Federal Initiatives in property insurance should place state and regional companies on an equal footing with large national ones.

I am here to express our support for efforts, particularly those of Representatives Lazio and McCollum, to draft legislation to better prepare for extremely large and devastating natural disasters.

For the Southern Farm Bureau Group, capital, reinsurance and financial markets are providing the capacity needed to manage most catastrophes. However, exposure to a mega catastrophe in highly populated or concentrated areas cause significant concern to our group of companies and to the industry.

The Federal Government can play a very constructive role, in partnership with the states and the insurance industry, in assuring that the insurance system has sufficient resources to honor obligations to consumers in their time of need and, equally importantly, has the ability to function after the disaster with a minimum of disruption to consumers, the industry and the financial markets.

We believe that:

- Federal programs should compliment, rather than replace, private sector capacity.
- No program should create a market advantage for certain segments of the insurance industry, or for government sponsored pools, over the private sector.
- Federal efforts should facilitate the emergence of new capital market products that have the potential to diversify risk throughout the world financial system.
- Federal efforts should not interfere with the traditional role of states as the primary regulators of insurance.

H.R. 219 as reported by the Subcommittee on Housing and Community Outreach is a well-intended step in the right direction. We want to continue to support the bill as it moves forward. However, we believe H.R. 219 can be strengthened in order to:

- increase the likelihood that policyholders in disaster prone areas will have insurance claims fully paid in the event of large catastrophic events;
- increase insurance industry capacity so that the number of homeowners able to adequately insure their homes and possessions is maximized:
- assure that insurers of all sizes and in every marketing area will be in a financial position to pay catastrophic disaster claims and be able to respond to future catastrophic events.

We were pleased to see that the Subcommittee, in reporting H.R. 219, included provisions for excess-of-loss catastrophic reinsurance contracts.

Having participated in the creation and implementation of the Florida Hurricane Catastrophe Fund, I can attest to the challenges that may face other states if they elect to create state funds. While Florida's Catastrophe Fund is an excellent example of a state program that has complimented the private sector and provided considerable claims paying capacity to the system in a financially sound manner, what has worked in states with the most severe problems may not be best for the rest of the country. Many states may not have the financial base or expertise to support such a mechanism.

For this reason, we agree with the Subcommittee that Federal Excess of Loss Contracts would afford property insurers a valuable secondary source to the private sector for high level disaster insurance protection. Contracts should be made available to insurers and state programs directly by the Federal Government. This would allow the government to enhance claims paying capacity in many states without the need for additional state government programs, while not interfering with states' ability to maintain existing programs or to create new ones.

We strongly agree with the Subcommittee that the state level is the most appropriate geographic focus for the sale of reinsurance contracts and disagree with those who have argued that such contracts should only be made available on a national basis. Contracts must be structured in a way to be useful to regional and single-state insurers.

While several insurers market their property insurance coverage on a national basis in most or all states, the substantial majority of property insurance companies operate in only one or a handful of states. National contracts help only one segment of the large and diverse insurance industry. The advantage of single-state contracts is that insurers only would need to purchase contracts for the state or states in which they have a catastrophic exposure.

We urge the Banking Committee to adopt the concept contained in H.R. 219 for auctions of Treasury Excess of Loss Reinsurance Contracts on a state-by-state basis so that single state or regional insurance companies can participate without having to bid on what are likely to be more expensive national contracts. Contracts could be allocated to states by the Treasury Department based in the probability of a catastrophic event occurring in the state and the premium volume of insuring entities doing business in the state. Regional and single state insurance companies bear significant risk in many disaster prone states and often fill gaps in coverage not written by large national writers. They should be able to fairly participate in the program.

The Subcommittee made a sincere effort to address this concern by including in Sec. 4 of H.R. 219 a provision for "State Auction Programs." However, we think this provision may be unworkable. At this time, no state has enacted, nor has any state proposed legislation to provide for a state auction program. Some states have a severe exposure to one or more catastrophic natural disaster peril, even though a catastrophic event has not occurred for a century or more. It could be difficult for legislatures in some of these states to appreciate the magnitude of the exposure to their residents. State auction programs likely would vary in context, application and consistency. Furthermore, H.R. 219's current requirement for the states to create and administer "state auction programs" adds an unnecessary and expensive requirement that states act as intermediaries between the U.S. Treasury and private insurers.

We strongly urge that H.R. 219 be amended to simply allow insurers and reinsurers to purchase Excess of Loss Reinsurance Contracts direct from the U.S. Treasury Department. We believe that this change will bring broader industry support for H.R. 219.

There has been a great deal of debate over the amount of retained losses for insurers, or, as it is commonly stated, the trigger for U.S. Treasury Excess of Loss Reinsurance Contracts. We believe that Treasury contracts should be triggered by substantial losses which would threaten the solvency of the insurance industry and its ability to continue to serve policyholders. Triggers for individual states should vary according to the probability of catastrophic events and the size of the state insurance market. Interestingly enough, H.R. 219 does this for the Hawaii Fund. Triggers should be established as a part of the Treasury Department contracts with the advice of the Loss Cost Commission created by H.R. 219.

We believe that a system of state auctions of U.S. Treasury Excess of Loss Contracts can be developed which will not compete with the private capital market and could be structured to actually complement the private market by providing a needed high layer of catastrophe reinsurance above the private market. The Secretary of the Treasury should be charged with the duty of taking into consideration developments in the capital marketplace when he establishes an Excess of Loss Reinsurance program under this legislation.

The Loss Cost Commission is an important part of this legislation and will ensure that expertise will be available to the Treasury to price the product to reflect exposure.

Consumers in many states are facing property insurance availability problems, which could explode after the next catastrophic event if the insurance system's financial solidity is damaged. This issue is critically important, and should be a high priority for Congress and the Administration

We appreciate this opportunity to convey our support for the concepts contained in H.R. 219 and to make our recommendations for improving and strengthening the bill.

Thank you.